DE 03-175

PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE

Petition for Approval of Transition Service Rate as of February 1, 2004

Order Following Hearing

ORDER NO. 24,252

December 19, 2003

APPEARANCES: Gerald M. Eaton, Esq. for Public Service Company of New Hampshire; McLane, Graf, Raulerson & Middleton, P.A. by Steven V. Camerino, Esq. for Constellation New Energy, Inc. and Constellation Power Source, Inc.; James T. Rodier, Esq. for Freedom Partners, LLC d/b/a Freedom Energy; Office of Consumer Advocate by F. Anne Ross, Esq. on behalf of residential ratepayers; and Donald M. Kreis, Esq. of the Staff of the New Hampshire Public Utilities Commission.

I. PROCEDURAL HISTORY

On September 12, 2003, Public Service Company of New Hampshire (PSNH) filed with the New Hampshire Public Utilities Commission (Commission) a petition to establish PSNH's Transition Service rate for 2004. Pursuant to the relevant provision of the Electric Industry Restructuring Act, RSA 374-F:2, V, Transition Service is "electricity supply that is available to existing retail customers prior to each customer's first choice of a competitive electricity supplier, and to others, as deemed appropriate by the commission."

For certain commercial and industrial customers of PSNH, the currently applicable Transition Service rate was set in Order No. 24,117 (January 30, 2003) at 4.67 cents per kilowatt-hour. For the remainder of PSNH's customers, the current Transition Service rate is fixed by RSA 369-B:3, IV(b)(1)(B)(i) at 4.6 cents per kilowatt-hour. Pursuant to RSA 369-B:3, IV(b)(1)(C), as of February 1, 2004, the Transition Service rate for all PSNH customers shall be "PSNH's actual, prudent and reasonable costs of providing such power as approved by the commission."

According to the pre-filed direct testimony appended to the PSNH petition, PSNH made a "preliminary calculation" that PSNH's reasonable and prudent cost of providing Transition Service in 2004 would be 5.13 cents per kilowatt-hour. Prefiled Testimony of Robert A. Baumann at 3. In the cover letter accompanying the petition, PSNH notes that it expects the proposed rate would be revised over the course of the proceeding to reflect updated estimates of fuel and energy prices.

The PSNH petition makes certain additional requests: (1) that the rate for Default Service continue to be equal to the Transition Service Rate, see RSA 374-F:I-a (defining Default Service as "electricity supply that is available to retail customers who are otherwise without an electricity supplier and ineligible for transition service"), and (2) that the Commission revise its requirement as to the coal inventory PSNH must maintain at its Merrimack and Schiller generation stations. According to PSNH, reducing the amount of required coal inventory would be prudent and would also reduce PSNH's fuel costs, a savings that would inure to the benefit of PSNH customers via the Transition Service and related stranded cost recovery mechanisms.

The Commission entered an Order of Notice on September 23, 2003, scheduling a Pre-Hearing Conference for October 10, 2003 and establishing a deadline of October 7, 2003 for intervention petitions. The Office of Consumer Advocate (OCA) entered an appearance on behalf of residential ratepayers. The Commission received intervention petitions from Constellation NewEnergy, Inc. and Constellation Power Source, Inc. (appearing jointly and hereinafter referred to jointly as "Constellation") and Freedom Partners, LLC d/b/a Freedom Energy (Freedom Energy).

The Pre-Hearing Conference took place as scheduled. At the Pre-Hearing Conference, the Commission granted the pending intervention requests without objection. Following the Pre-Hearing Conference, the parties and Commission Staff conducted a technical session and agreed upon a proposed procedural schedule. The Commission approved the proposed schedule by secretarial letter on October 24, 2003. The schedule provided for a merits hearing on November 21, 2003.

Discovery ensued. The parties and Staff conducted an additional technical session and settlement conference on October 30, 2003. By secretarial letter dated November 12, 2003, the Commission advised the parties that the merits hearing had been rescheduled to December 3, 2003. The parties and Staff conducted a settlement conference on November 19, 2003. On November 21, 2003, the Commission received pre-filed direct testimony from witnesses for Constellation and Staff. The merits hearing took place as scheduled on December 3, 2003.

On December 5, 2003, PSNH submitted a revised calculation of its proposed Transition Service rate, based on market conditions as of the hearing date (December 3, 2003). These revised calculations yielded a Transition Service rate of 5.36 cents per kilowatt-hour.

In light of the December 5 filing, the Commission on December 9, 2003 transmitted certain record requests to PSNH. These record requests sought details and the underlying basis of PSNH's revised Transition Service rate calculation. PSNH filed a timely response to the record requests on December 11, 2003.

II. POSITIONS OF THE PARTIES AND STAFF

A. Public Service Company of New Hampshire

PSNH notes that, pursuant to RSA 369-B:3, IV(b)(1)(C), as of January 31, 2004 the price of Transition Service for all PSNH customers must be based on PSNH's "actual, prudent and reasonable" costs of providing such service. PSNH further notes that, under the revenue recovery methodology contained in the Agreement to Settle PSNH Restructuring (Restructuring Agreement) and related legislation, PSNH's Transition Service revenues are compared to PSNH's Transition Service costs, with the net of the two resulting in an adjustment to PSNH's Part 3 stranded costs.[1]

PSNH is requesting that the Commission approve a fixed Transition Service rate that would be applicable on a bills-rendered basis from February 1, 2004 through January 31, 2005. At the time it made its original filing in this docket, PSNH estimated that its actual, prudent and reasonable cost of providing Transition Service from February 1, 2004 through January 31, 2005 would be 5.13 cents per kilowatt-hour. [On October 29, 2003, PSNH circulated to the parties and Staff a revised calculation yielding a Transition Service rate of 5.23 cents.] According to PSNH, its original estimate (and presumably the October 29 figure as well) exceeds the current Transition Service rate of 4.67 cents applicable to certain commercial and industrial customers, and the 4.6 cents applicable to other customers, due to "an overall increase in PSNH generating unit dispatch prices driven by higher commodity prices for fuel and increased [operating and maintenance] costs due in part to additional scheduled planned maintenance activities at PSNH's

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[1] Under the Restructuring Agreement, Part 3 stranded costs are those stranded costs for which PSNH assumed some risk of non-recovery at the time the Restructuring Agreement was signed in 1999. In other proceedings, PSNH has indicated that it expects to recover all Part 3 stranded costs, with recovery completed at some point in 2006.

generating units." Pre-filed testimony of Robert A. Baumann at 4.

To reach its proposed Transition Service rate, PSNH calculated its projected fossil energy costs for the period, operations and maintenance costs (including depreciation expenses and taxes) associated with its generation portfolio, a return on applicable rate base, certain additional costs paid through the Independent System Operator, costs related to PSNH's Vermont Yankee power purchase entitlement and obligation, costs related to PSNH's mandated purchases from Independent Power Producers (IPPs) in its service territory, and the net of PSNH's energy purchases and sales in the regional electricity market. The sum of these figures was divided by PSNH's forecasted retail sales in megawatt-hours to reach its proposed Transition Service rate. PSNH valued its mandated IPP purchases using projected market costs (both as to energy and capacity). PSNH proposes no separate reconciliation of actual Transition Service costs. Rather, consistent with Order No. 24,224 (October 24, 2003) reconciling PSNH's Stranded Cost Recovery Charge (SCRC) for 2002, PSNH proposes that transition service costs for the upcoming year be reconciled in the SCRC proceeding. PSNH regards changing the Transition Service rate on a bills-rendered (as opposed to a service-rendered) basis to be appropriate because the rate is fully reconcilable in the SCRC proceedings and because this is consistent with Transition Service rate changes in the past.

The other major issue raised by PSNH concerns the coal inventory it is required to maintain at its two facilities that burn coal, the Merrimack and Schiller stations. PSNH is presently obliged to maintain a 60 day supply at Merrimack Station from February through November, a 70-day supply during December and January and a 90-day supply at a time when the labor contract of its supplier is due to expire which, raises the possibility of a coal strike. *See Public Service Co. of N.H.*, 65 NH PUC 312, 313 (1984). At Schiller Station, PSNH is required to maintain a 45 to 60-day supply. *See Public Service Co. of N.H.*, 65 NH PUC 673, 675 (1984).

PSNH witness Jody J. TenBrock testified that PSNH has a longstanding relationship with the principal fuel supplier for Merrimack Station, Consolidated Coal Company (CONSOL). According to Mr. TenBrock, in 1984 PSNH experienced severe cash constraints and therefore interrupted payment to CONSOL for the coal supply. Mr. TenBrock stated that this caused CONSOL to interrupt coal shipments, which led to a Commission investigation and, ultimately, to the imposition of minimum inventory requirements by the Commission.

Mr. TenBrock noted that Merrimack Station uses an average of 3,000 to 3,300 tons of coal per day. He explained that Merrimack uses cyclone boilers that require types of coal that melt at low temperatures, thus limiting the range of potential supply. According to Mr. TenBrock, Merrimack's coal supply is predominantly "mid-sulfur coals" from domestic sources, blended with low-sulfur coals from both foreign and domestic sources for the purpose of allowing the facility to comply with applicable sulfur dioxide emissions limits. Pre-Filed Testimony of Jody J. TenBrock at 3.

Mr. TenBrock testified that in order to get the domestic coal to Merrimack Station, PSNH leases two train sets with 100 rail cars, with other train sets potentially available. He said that transit time from the mines to Merrimack Station range from two to ten days. He noted that foreign, low-sulfur coal is delivered to Schiller Station, where it is off-loaded from ocean-going barges and then taken by truck to Merrimack Station. These truck deliveries of approximately 1,000 tons per day "can be accomplished on an unhurried eight hour a day schedule, five days per week." *Id.* at 4.

According to Mr. TenBrock, if the rail supply to Merrimack were interrupted, it would be possible for domestic low-sulfur coals to be sent via rail to ports on the Chesapeake or Delaware Bays and barged to Schiller for transport to Merrimack. He testified that around-the-clock trucking from Schiller to Merrimack could provide the 3,000 to 3,300 tons per day that Merrimack burns. He noted that PSNH has also used Providence, Rhode Island and New Haven, Connecticut as ports for off-loading coal that can then be trucked to Merrimack Station.

Mr. TenBrock further noted that Schiller Station uses between 1,100 and 1,400 tons per day of high fusion, low-sulfur coals that arrive via barge from Appalachian and South American mines. He noted that all three Schiller boilers can also be fired with oil, of which there are 700,000 barrels stored between Schiller and PSNH’s nearby Newington Station. He also noted that, as with Merrimack, coal from foreign sources could be offloaded at other New England ports and trucked to Schiller Station. Mr. TenBrock further testified that domestic supplies for Schiller could arrive at Merrimack Station by train where they could then be trucked to the Schiller facility.

Mr. TenBrock offered testimony about what the two coal-burning facilities could do in the event of a coal supply interruption at the mine. According to Mr. TenBrock, there are other CONSOL mines, as well as other suppliers, that could be used on a temporary basis to supply Merrimack. He noted that the CONSOL facilities are not unionized and, thus, that a miners’ strike is not a possibility there. He testified that the possibility of a rail strike would be known months, if not a full year, ahead of time, amply allowing for alternative arrangements.

Finally, Mr. TenBrock testified that the majority of coal for that facility has come in recent years from Venezuela and Colombia. He noted that, in the face of political turmoil and related strikes in Venezuela earlier this year, Schiller was easily able to switch to Colombian coal.

In its pre-filed direct testimony, PSNH proposed to maintain smaller coal supplies at both plants, a minimum 30-day supply at Schiller and a 45-day supply at Merrimack. According to PSNH, this would save customers $330,000 per year by reducing PSNH's carrying costs associated with its coal inventory. PSNH indicates that it would be willing, as a condition of approving this change, to be required to build inventories to 90 days at Merrimack and 60 days at Schiller in anticipation of any strikes or other events that could interrupt coal supply or transport.

At hearing, in response to Staff's concern about the coal supply issue, Mr. TenBrock revised PSNH's proposal with regard to coal inventory requirements. Specifically, PSNH proposed the maintenance of the 45- to 60-day inventory requirement at Schiller Station, but based on an "average minimum inventory" level that takes into account inventory spikes resulting from large seaborne shipments. PSNH further proposed that the inventory requirement for Merrimack Station be lowered to 45 days. And, finally, PSNH proposed a 30-day minimum inventory requirement for Schiller that would apply to the collective supplies available at both stations,[2] to take into account the relative ease with which coal can be moved between them.

B. Constellation NewEngery, Inc. and Constellation Power Source, Inc.

According to Constellation, since the implementation of restructuring in PSNH’s service territory in 2001, PSNH’s Transition Service rate has significantly understated the actual cost of providing this service. Constellation notes that the resulting under-recovery is reflected in PSNH’s recoverable, Part 3 stranded costs. According to Constellation, this results in unnecessary harm both to PSNH’s customers and to the development of a competitive electricity market in New Hampshire. Constellation further contends that a variable Transition Service rate would send better price signals to customers, would more accurately reflect PSNH’s actual cost of providing Transition Service and would further support the development of a competitive market.

Constellation points out that competitive suppliers must reflect their full costs in the prices they charge, whereas under the current Transition Service paradigm PSNH is able to avoid doing so. Constellation further contends that when PSNH recovers costs associated with Transition Service via other

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[2] The amount of coal inventory at Merrimack Station that would potentially satisfy this requirement would only be the amount in excess of Merrimack’s required inventory.

charges (i.e., distribution and stranded cost charges), customers migrating to a competitive supplier in effect pay twice – by compensating PSNH for some of its energy costs and compensating the competitive supplier for energy costs as well. In addition, according to Constellation, under PSNH's proposal the comparison between competitive supply and PSNH's Transition Service will be skewed and, therefore, a competitive market would be unlikely to develop.

It is Constellation's contention that PSNH's proposed Transition Service rate does not reflect PSNH's full cost of providing the service for the following reasons. First, Constellation notes that PSNH's proposed rate is based on forecasts – and the actual costs incurred by PSNH inevitably will vary from such forecasts. Second, Constellation contends that the Transition Service rate as proposed by PSNH does not reflect the full administrative and other costs of providing the service. According to Constellation, the Commission can and should correct this second problem in Docket No. DE 03-200 (the upcoming rate case with respect to PSNH's Delivery Service charge), something Constellation believes can be accomplished on a revenue-neutral basis to PSNH.

Third, Constellation contends PSNH's Transition Service rate should include more costs associated with IPPs than it currently does. Noting that the Commission did not accept this proposition when setting PSNH's Transition Service rate for large commercial and industrial customers effective February 1, 2003, *see* Order No. 24,117 (January 30, 2003), Constellation contends that either the Commission or the Legislature should revisit this issue at an appropriate juncture. Similarly, Constellation invokes the testimony it submitted in that proceeding with respect to its argument about certain PSNH costs that are not but should be reflected in the Transition Service rate.

Constellation advocates that the Commission should address the forecast inaccuracy problem by requiring PSNH to establish as much of its Transition Service costs in advance as possible, through forward purchasing and other mechanisms, and praised PSNH for locking in a large portion of its fuel costs in advance. However, Constellation faults PSNH for not taking similar measures with respect to purchased power. Constellation notes that PSNH has engaged in at least some hedging with respect to purchased power, but cannot assess the details because of confidentiality restrictions imposed by PSNH.

Constellation argues that what is supposedly a fixed Transition Service rate for PSNH customers actually varies, with the variable component added after the fact via the stranded cost recovery mechanism. According to Constellation, costs are then shifted from Transition Service customers to migrating customers and any customers PSNH picks up during the period of after-the-fact cost recovery.

Constellation proposes that PSNH be required to fix its Transition Service costs in advance via a forward contract solicitation with respect to the entire PSNH Transition Service load, including the output from PSNH's owned generation and IPP entitlements. Specifically, Constellation believes PSNH should issue a request for proposals (RFP) for full requirements load-following service at a nominal price for the entire Transition Service load. Under this proposal, PSNH would provide information in its RFP as to the historical Transition Service load requirements, its IPP entitlements and the operating costs and unit characteristics of its owned generation facilities. Bidders would be required to accept the output from the IPPs and the PSNH owned generation and state a price for serving the load net of the IPP contract payments and the fuel and operating costs of the PSNH plants when dispatched.

According to Constellation, this approach – as opposed to having PSNH simply solicit bids for the net power requirement – can be easily implemented via the ISO New England settlement process. Constellation states that PSNH's Transition Service load is presently represented as an obligation within the ISO New England settlement system as a "load asset," for which PSNH is responsible. According to Constellation,

> [i]n order to have a third party supplant those wholesale purchases with a load-following product at a fixed forward price it is necessary to transfer a wholesale settlement obligation for that hourly net load above the entitlements and output. Separating that load and creating a metered load asset for it may not be possible. We believe the most practical approach is to transfer the entire transition service load asset along with the entitlement output and the plant output.

Pre-Filed Testimony of Bruce McLeish and Daniel W. Allegretti at 13. According to Constellation, this proposal is not unique and, in fact, is the norm in the service territories of Granite State Electric Company (which is served for Transition Service purposes by Constellation Power Source) and Unitil. Further, according to Constellation, there have been RFPs which included the provision of partial supply, with dispatch and scheduling rights, along with a request for full requirements service in connection with NStar, Central Maine Power Company, Bangor Hydro Electric Company and Unitil.

Constellation further contends that its proposal is consistent with the statutory requirement that PSNH serve its Transition Service load with its generation portfolio. According to Constellation, the approach it proposes has been used where similar restrictions apply in other jurisdictions. Constellation Power Source routinely provides requirements service to municipal utilities that have power entitlements from the New York Power Authority which must be used to serve municipal customers. According to Constellation, this obligation is effected through a load asset contract transfer that allows the value of the power entitlement to continue to benefit the relevant customers with the balance of the requirement supplied by Constellation Power Source, which assumes the ISO settlement obligation.

Constellation contends that Transition Service customers would not pay more for price certainty under its proposal. According to Constellation, the customers would pay a competitive, market-based forward price for power acquired in the regional market while no longer being exposed to the risks of what Constellation characterizes as a potentially volatile and uncertain spot energy price. Constellation concedes that "any reasonable supplier will include some cost factor in its bid that reflects the risk it is facing of providing service at a fixed price," McLeish and Allegretti Testimony, p. 14, and that Transition Service customers would see this cost factor added to their energy bill. However, Constellation posits the existence of an offsetting economic benefit because the supplier would not be able to impose additional charges at a later date if actual costs exceed the fixed price, something PSNH presently does through the stranded cost recovery mechanism.

Constellation conceded in its pre-filed testimony that it may not be possible to implement its proposal in time for

Transition Service delivered as of February 1, 2004. Therefore, Constellation asks the Commission to require PSNH to prepare an RFP, submit it to the Commission for review and, thereafter, issue it for service to customers effective on February 1, 2005. Under such an approach, according to Constellation, if none of the bids yielded a reasonable rate, the Commission could reject the bids and direct PSNH to continue to supply Transition Service under the present paradigm or in such other manner as is deemed reasonable.

At hearing, however, Constellation stated that it would be possible to implement its RFP proposal in time for the February 1, 2004 commencement of the upcoming Transition Service period.

Finally, and in the alternative, Constellation takes the position that because PSNH’s power cost varies from month to month, the Commission should require PSNH to set its Transition Service rate on a monthly basis, or at least a seasonal basis. According to Constellation, this would not require multiple proceedings before the Commission because the monthly prices could all be fixed at the outset of the period in a single proceeding comparable to the present case.

C. Freedom Partners, LLC d/b/a Freedom Energy

Freedom Energy did not offer testimony. However, Freedom Energy indicated through counsel at hearing that it believes the Commission should not adopt a variable price for PSNH's Transition Service. According to Freedom Energy, such variable pricing could complicate the marketing of the PSNH Retail Energy Services program approved by the Commission in Order No. 24,240 (Nov. 21, 2003), designed to stimulate migration of large customers to competitive suppliers by providing a credit that varies with PSNH's expected marginal Transition Service cost.

D. Office of Consumer Advocate

The OCA did not offer testimony. However, the OCA indicated its general agreement with the approach reflected in PSNH's proposal, with certain modifications. Specifically, the OCA proposed that PSNH be required to file periodic status reports, updating both its actual Transition Service costs and its forecast costs for the remainder of the period. OCA further proposed that the Commission be authorized to adjust PSNH's Transition Service rate based on the updated figures by up to 20 percent, but only once during the Transition Service period.

E. Staff

Staff indicates that it does not oppose the methodology used by PSNH to calculate its proposed Transition Service rate, given that it is identical to the methodology approved in Order No. 24,117. However, Staff recommends that the Commission reject PSNH's proposal with respect to required coal inventory.

According to Staff, on two previous occasions the Commission has declined to allow PSNH to reduce its coal inventory. *See Public Service Co. of N.H.*, 75 NH PUC 225 (1990) and *Public Service Co. of N.H.*, 80 NH PUC 1 (1995). Staff notes that PSNH has described a variety of coal sources and delivery methods that PSNH believes warrant reduction of coal supply at each facility. Staff recognizes that these tools are available; nevertheless, recent history suggests that PSNH's coal inventory levels are still quite vulnerable.

Specifically, according to Staff, during 2000 the coal inventory levels at both Merrimack and Schiller were below the required minimum levels for a significant portion of the year. Inventory levels were low at both facilities in 2001 as well. Staff concedes that, in 2002 and in 2003 at Merrimack Station and in 2003 at Schiller, coal inventory levels were consistently high.

What Staff characterized as the most glaring area of concern is the daily coal pile inventory at Schiller Station. According to Staff, citing data supplied by PSNH, at the end of April and during the beginning of May in 2002, Schiller Station was within a few days of running out of coal. Staff reports that PSNH attributes this to a shipment problem. Regardless of cause, according to Staff, the drop in inventory was due to one of the many risks that PSNH is now claming to be mitigated by a range of supply and delivery options.

According to Staff, the $330,000 in savings that PSNH estimates would result from its inventory proposal would be quickly offset in the event that the lack of coal supply required a switch to higher-priced oil or a shutdown and resulting energy purchases from the regional market. Staff stresses that it is not contending that PSNH has failed to manage its coal inventory properly – only that the proposed changes in inventory levels are not warranted on the present record.

However, Staff witness Steven Mullen suggested in his pre-filed submission that the Commission consider revising the requirement with respect to the 45 to 60-day inventory requirement at Schiller Station. According to Staff, Schiller Station uses 1,200 tons of coal per day, with an additional 1,000 tons per day trucked from Schiller Station to Merrimack Station. According to Staff, a 40,000 ton shipment of coal delivered to Schiller Station represents roughly 18 days of coal for both plants, based on the daily consumption of Schiller and the daily trucking to Merrimack, or 33 days for Schiller alone. Staff points out that shipments of this magnitude lead to wide swings in the inventory levels at Schiller. Thus, according to

Staff, requiring a minimum coal inventory of 45 to 60 days at Schiller Station may mean that at times, particularly right after a large shipment, PSNH has much more coal on hand than is reasonably necessary. Staff suggested that the Commission consider establishing some kind of "average minimum" or other means of determining an appropriate minimum inventory level for Schiller Station.

Finally, Staff notes that the current coal inventory requirements were imposed at a time when PSNH was experiencing financial conditions that are less favorable than those PSNH currently experiences. Thus, according to Staff, it may be time to take a fresh look at whether all minimum coal inventory requirements should be eliminated at some point in the future. Staff notes that, in such circumstances, PSNH would still be required to conduct its fuel procurement efforts in a prudent manner or risk non-recovery of any related costs.

At hearing, Mr. Mullen testified that Staff was satisfied with PSNH's revised proposal as articulated by Mr. TenBrock in his live testimony.

III. COMMISSION ANALYSIS

a. Statutory Framework

Nearly a year ago, in Order No. 24,117, the Commission approved a Transition Service rate of 4.67 cents for certain large commercial and industrial customers of PSNH, marking the first time that any PSNH customers were subject to a Transition Service rate based upon the utility's "actual, prudent and reasonable costs" of providing the service. *See* RSA 369-B:3, IV(b)(1)(C). February 1, 2004 marks the "initial transition service end day" within the meaning of RSA 369-B:3, IV(b)(1)(B)(i). Accordingly, there is no longer a legislatively determined Transition Service rate that is applicable to PSNH and, for the first time, the Commission is required to apply the 'actual, prudent and reasonable' cost standard in establishing a Transition Service rate for all PSNH customers. *See id.* at (ii).

In Order No. 24,211, the Commission provided a detailed analysis of what it acknowledged to be a complicated statutory scheme that guides this determination, noting that in the case of PSNH the setting of Transition Service rates is affected in particular by the terms of the Restructuring Agreement. *See* Order No. 24,211, slip op. at 49-50 (summarizing analysis of legislation as applied to PSNH). The Commission then applied its view of the pertinent statutes to certain issues then in dispute. Specifically, the Commission decided that the above-market cost (as opposed to the market value) of the power PSNH is obliged to purchase from IPPs should not be reflected in the Transition Service price. *Id.* at 53-54, 62. And the Commission determined that certain of PSNH's administrative costs were properly included in PSNH's Delivery Service charge as opposed to its Transition Service rate. *Id.* at 63-64. Here, Constellation has again raised these issues, without adding any evidence to that which informed the Commission's determination in Order No. 24,211. Accordingly, the we decline to revisit those determinations.

The statutory landscape has shifted since Order No. 24,211 in one highly relevant respect. Specifically, the Legislature has enacted Senate Bill 170, which extended the earliest date upon which PSNH could sell its non-nuclear generation portfolio from February 1, 2004 to April 30, 2006, *see* 2003 N.H. Laws 29:4 (codified as RSA 369-B:3-a). The Legislature made clear that any such sale could only occur upon a finding by the Commission that "it is in the economic interest of retail customers of PSNH," *id.*, and clarified that before any such divestiture PSNH "*shall* supply all . . . transition and default service offered in its retail electric service territory from its generation assets" and additional purchases obtained under a Commission-approved method as necessary, *see id.* at § 2 (codified as RSA 369-B:3, IV(b)(1)(A)) (emphasis added).[3]

[3] The "shall supply" language was also in the previously applicable version of the statute; the revision eliminated references to the sale of PSNH's interest in the Seabrook nuclear power plant (completed in 2002) and made clear that the obligation to supply Transition and Default Service out of the PSNH non-nuclear generation portfolio would continue through the now-extended period for PSNH's ownership of these assets.

b. The Constellation Bid Proposal

It is against this revised statutory backdrop that we consider Constellation's proposal for PSNH to seek bids on its incremental Transition Service load (i.e., its Transition Service requirements net of the output of its generation assets and power entitlements). With regard to the "shall supply" language in RSA 369-B:3, IV(b)(1)(A), Constellation contends that PSNH would still be supplying Transition Service out of these assets even though the Constellation proposal would involve the transfer of these entitlements to the successful bidder for purposes of facilitating the settlement of PSNH's Transition Service load for dispatch and market settlement purposes. According to Constellation, under this scenario PSNH would still be supplying Transition Service at retail, while conducting its transaction with the successful bidder at the wholesale level.

We will not order PSNH to procure or supply Transmission Service according to the bidding process proposed by Constellation. We believe Constellation's proposal is inconsistent with RSA 369-B:3, IV(b)(1)(A). In our view, the plain language of this provision makes clear the Legislature's requirement that PSNH procure and supply Transition Service in precisely the manner PSNH proposes: by employing its generation portfolio directly for that purpose and making appropriate market purchases for its additional requirements.

Moreover, we are required to read this provision in its overall context, and in a manner that advances the statute's purposes considered as a whole. *See, e.g., New Hampshire Div. of Human Servs. v. Hahn*, 133 N.H. 776, 778 (1990); Order No. 24,211, slip op. at 25. Reading this provision in the context of the provision requiring PSNH to price its Transition Service according to its actual costs (if such costs are also prudent and reasonable) leads to the conclusion that the Legislature intended PSNH to use its generation portfolio directly for the benefit of its Transition Service customers, as opposed to consigning them to a third party for resale to PSNH's customers.

It is also our finding that, even assuming Constellation's proposal was permissible under the statute, the record does not demonstrate that it would yield prudent and reasonable Transition Service prices. This is because of the likelihood that PSNH customers would pay more for PSNH-generated power under Constellation's bidding proposal than they would under PSNH's plan to use these resources directly to serve retail load. For instance, under the PSNH arrangement any forced outages at the PSNH generation facilities resulting from imprudence would not be recoverable from customers. In the alternative, under Constellation's paradigm the third-party bidder would assume all risks associated with forced outages and, presumably, increase the bid price accordingly. Consequently, in comparing the two models it is fair to conclude that there would be no observable economic benefit to ratepayers from the Constellation paradigm. More generally, Constellation has not demonstrated how interposing a third party between PSNH generation and PSNH Transition Service customers will not inevitably lead to a higher price for PSNH-generated power since under such a paradigm there will be not one but two companies seeking to earn a return on this power supply as well as two companies incurring overhead and administrative costs. This is consonant with the Commission's previous observation that "it is not economically efficient for PSNH to sell its generation capacity into the regional wholesale market and then buy back its Transition Service-related needs." *Id.* at 60.

c. Variable Pricing

We will not adopt Constellation's proposal for so-called variable Transition Service pricing that employs monthly or seasonal prices. While potentially valid in concept, such a pricing methodology is unlikely to provide meaningful and appropriate price signals to PSNH customers given that market energy prices and PSNH's costs of providing Transition Service reflect non-coincident trends over the course of a year.

Such a plan would require the normalization of PSNH's costs related to plant maintenance, which would eliminate price spikes during the "shoulder" months in spring and fall that are typically devoted to such work. It was clear at the hearing that after such normalization, PSNH's Transition Service costs would be only minimally higher in summer than they would be in winter.

In Order No. 24,211, the Commission explicitly did not rule out a variable Transition Service price for PSNH customers. *See id.* at 66. The Commission indicated, however, that any such plan must strike an appropriate balance among the restructuring policy principles set forth in RSA 374-F:3, particularly "the option of stable and predictable ceiling electricity prices" during the transition to retail competition that is also consistent with the principle of near-term rate relief. Order No. 24,211, slip op. at 65-66, quoting RSA 374-F:3, V(b). We are not convinced that varying the price modestly in summer would send a significant enough price signal to justify such a step away from stable prices. Further, Staff noted, the Commission has never approved a variable Transition Service rate for residential customers and moving down the path proposed by Constellation would require it to examine the effect of such an innovation on the various classes of PSNH customers.

d. Avoidance of Deferrals

In its discussion of the benefits of setting the Transition Rate as nearly as possible to actual costs, Constellation points out that under the current method there has been a significant underrecovery that resulted in deferring costs to the Stranded Cost Recovery Charge. Although we have concluded that Constellation's specific proposal is not the appropriate remedy, we are persuaded that steps should be taken to lessen the likelihood of deferrals. This is a policy imperative that the Legislature has specifically endorsed, albeit in the context of legislation that assumed complete divestiture of PSNH's generation assets and acquisition of Transition Service power by other means. *See* RSA 369-B:3, IV(b)(1)(E) (instructing that, except as specifically provided by statute, Commission "shall not accept any [Transition Service provider's] bid or implement any pricing strategy for transition service that creates any deferrals").

Avoiding deferrals arising out of Transition Service was an objective that the Commission unambiguously embraced when it approved the PSNH Restructuring Agreement in 2000. *See* PSNH *Proposed Restructuring Settlement*, 85 NH PUC 154, 252, 253 (2000) (adjusting initial Transition Service prices in Restructuring Agreement upward to minimize risk of deferrals and noting that requiring PSNH to provide Transition Service from its owned generation assets would also contribute to that end). We agree with the OCA that avoiding deferrals remains sound policy because, in general, the customers taking Transition Service from PSNH between February 1, 2004 and January 1, 2005 should be the customers who pay the associated costs.

OCA proposes that the Commission allow, upon request of a party or Staff, a one-time adjustment to the Transition Service price, between February 1, 2004 and January 31, 2005, of up to 20 percent. In our judgment, the relevant policy principles expressed in RSA 369-B and RSA 374-F:3 would be better served by a somewhat different approach – one that is more flexible as to price and more temporally predictable. Specifically, it is our determination that, upon request of any party or Staff, PSNH's Transition Service rate will be revisited in July 2004 with an eye toward a possible adjustment in the price effective on August 1, 2004. We choose that date because it would allow consideration of actual cost data from four months of this Transition Service period which will capture the 'shoulder' period in which PSNH's generation facilities typically undergo planned maintenance outages, as well as updated cost forecasts for a significant remainder of the Transition Service period.

What we envision would potentially be conducted in July of 2004 is a proceeding similar to the "cost of gas" rate adjustment proceedings routinely conducted for gas utilities. In other words, it is not our intent to reopen the full menu of issues that are expected to be considered again at the end of the next Transition Service period one year from now. Rather, should a petition be filed and granted, review will be limited to a consideration of whether it is in the public interest to adjust the transition service rate using the methodology we approve today.

In the initial reconciliation of the Stranded Cost Recovery Charge (SCRC) authorized by the Restructuring Agreement, the Commission approved a settlement that required PSNH to make quarterly reconciliation filings that report on, inter alia, PSNH's Transition Service costs. *See* Order No. 24,125 (February 14, 2003). We realize that our willingness to consider adjusting the Transition Service price on August 1, 2004 may require a modification of this reporting schedule. Accordingly, we direct PSNH to confer with the other parties and Staff with an eye toward reaching an agreement in light of this order on any necessary revisions of both the data PSNH reports over the course of the year and the timing of those reports. We direct Staff to submit a report of such discussions by March 1, 2004.

At hearing, PSNH took the position that in the event of a revision of the Transition Service price during the upcoming year, it would be inconsistent with the Restructuring Agreement to apply any over- or under-collections to PSNH’s Transition Service account as opposed to Part 3 stranded costs. We find no language in the Restructuring Agreement that precludes PSNH from applying any over- or under-collections from the current Transition Service year in calculating a revised Transition Service price for the remainder of the year. This is hardly surprising, since the present situation – a potentially long-term retention by PSNH of its non-nuclear generation assets and their continued use for PSNH’s Transition Service – was obviously not a circumstance contemplated by the parties to the Restructuring Agreement when they signed the document in 1999.

Rather, we find the relevant limitation to be the Legislature’s subsequently enacted requirement that Transition Service be priced according to PSNH’s actual, prudent and reasonable costs. Allowing for one mid-course correction during the upcoming Transition Service year does not violate the requirement to apply actual costs because it leaves unchanged the annual practice of applying over- or under-collections related to Transition Service to Part 3 stranded costs. We express no view at this time about whether Transition Service under- or over-collections could be carried forward to future Transition Service years as opposed to being applied to stranded costs.

In light of the foregoing, the potential Transition Service price revision on August 1, 2004 will be solely a result of changes in the reported historical data and forecasted estimated data and will not be due to any changes in the methodology that the Commission approved in Order No. 24,211.

e. Coal Inventory

The only remaining issue concerns the proposed revision of the coal inventory requirements with respect to PSNH's Merrimack and Schiller stations. This issue is easily resolved.

It is undisputed that PSNH no longer confronts the circumstances that led to the imposition of coal inventory requirements in the first place, i.e., interruptions in coal deliveries occasioned by PSNH's inability to pay for them. It is also undisputed that PSNH is able, with relative ease, to move coal between the two facilities and, therefore, that the coal inventories of each can be combined for the purposes of establishing any minimum inventory requirement. The proposal agreed to by Staff and PSNH would, in effect, ratify PSNH's current practices and take into account the fact that inventories at Schiller fluctuate significantly because it receives large-lot coal deliveries by barge. PSNH's current practices have obviously not led to any supply-related outages or curtailments, and any such events are subject to review for prudency in any event. In these circumstances, it is appropriate and reasonable to approve the proposal PSNH made at hearing.

Specifically, the coal inventory requirement at Merrimack Station shall be lowered to 45 days and PSNH shall maintain the current 45 to 60-day inventory requirement at Schiller Station, but based on an “average minimum inventory” level that takes into account inventory spikes resulting from large seaborne shipments.

In addition, Schiller shall have a 30-day minimum inventory requirement. The supply of coal at Schiller and the amount of coal at Merrimack in excess of its required inventory would be used to potentially satisfy this latter requirement. Finally, if PSNH anticipates any strikes or other events that could interrupt coal supply or transport, PSNH shall be required to maintain a 90-day supply of coal at Merrimack Station and a 60-day supply at Schiller Station.

We direct PSNH to keep Staff informed in the event that PSNH is at risk of noncompliance with any of the minimum inventory levels and to explain the circumstances surrounding such events. It causes concern that at some point, perhaps as a result of personnel changes within the Commission Staff, PSNH discontinued the practice of reporting to Staff whenever it expected coal inventories to fall below the requisite level.

Although hindsight reveals that any inventory deficiencies had no effect on service, we place PSNH on notice of the importance of timely reporting.

We also express a willingness to revisit this general issue next year and to consider eliminating the inventory requirement altogether if circumstances warrant.

Based upon the forgoing, it is hereby

ORDERED, that the petition of Public Service Company of New Hampshire, providing for a Transition Service rate of 5.36 cents per kilowatt-hour effective on February 1, 2004, is GRANTED IN PART and DENIED IN PART, as described fully herein; and it is

FURTHER ORDERED, that Public Service Company of New Hampshire shall submit a compliance tariff within three business days of the entry of this Order; and it is

FURTHER ORDERED, that the petition of Public Service Company of New Hampshire with respect to coal inventories at its Merrimack and Schiller generating stations, as modified at hearing, is GRANTED.

By order of the Public Utilities Commission of New Hampshire this nineteenth day of December, 2003.

Thomas B. Getz Chairman	Susan S. Geiger Commissioner	Graham J. Morrison Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary